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IN THE

Supreme Court of the United States

OCTOBER TERM, 1964

No. 731

NATIONAL LEAD COMPANY, *Petitioner*

v.

COMMISSIONER OF INTERNAL REVENUE

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

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The petitioner, National Lead Company, petitioner below, prays that a writ of *certiorari* issue to review the judgment of the Court of Appeals for the Second Circuit in the above-entitled case.

OPINIONS BELOW

The findings of fact and opinion of the Tax Court are reported at 40 T.C. 282. The opinion of the Court of Appeals for the Second Circuit is reported at 336 F. 2d 134, and the pertinent portion thereof is printed herein as Appendix A.

JURISDICTION

The judgment of the Court of Appeals for the Second Circuit, affirming the decision of the Tax Court in respect of the issues to which this petition is addressed, was entered September 1, 1964. The jurisdiction of this Court is invoked under Title 28, U.S.C., Sec. 1254(1).

QUESTIONS PRESENTED

The fundamental question presented, from which three subsidiary questions stem, is whether a sale of certain corporate shares, made by the petitioner in 1937 to its wholly-owned British subsidiary, in order (for all that appears) to establish a tax loss, must be treated, in open tax years subsequent to 1937, as never having been made at all. The subsidiary questions, and ultimate questions in terms of tax result, are:

(a) Whether the petitioner is entitled to deduct as an ordinary loss, the difference, arising out of British currency devaluation, between the dollar value when incurred in 1937, and the dollar value when repaid in 1952, of an indebtedness due it from its wholly-owned British subsidiary, in respect of the aforesaid sale of corporate shares.

(b) Whether the petitioner is required to include in its own gross income, in open tax years subsequent to 1937, dividends received by its wholly-owned British subsidiary in respect of the aforesaid corporate shares.

(c) Whether the petitioner is required to include in its own gross income, in open years subsequent to 1937, gains derived by its wholly-owned British subsidiary upon the sale by the subsidiary of some of the aforesaid corporate shares.

STATUTES INVOLVED

This case does not involve any construction of the language of statute or regulation. However, the provisions below are quoted, for reference, as those under which items of income are commanded to be included for tax; items of deduction are allowed; and permissible foreign tax credits are specified.

Internal Revenue Code of 1939, as amended:

SEC. 22. GROSS INCOME.

(a) *General Definition.*—"Gross income" includes gains, profits, and income derived from * * * dealings in property, whether real or personal, growing out of the ownership or use of or interest in such property; also from * * * dividends * * *, or the transaction of any business carried on for gain or profit, or gains or profits and income derived from any source whatever.

SEC. 23. DEDUCTIONS FROM GROSS INCOME.
In computing net income, there shall be allowed as deductions:

* * *

(f) *Losses By Corporations.*—In the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise.

SEC. 131. TAXES OF FOREIGN COUNTRIES AND POSSESSIONS OF UNITED STATES.

(a) *Allowance of Credit.*—If the taxpayer chooses to have the benefits of this section, the tax imposed by this chapter * * * shall be credited with:

(1) Citizens and Domestic Corporations.—In the case of a citizen of the United States and of a domestic corporation, the amount of any income, war-profits, and excess-profits paid or accrued during the taxable year to any foreign country * * *.

* * *

(b) *Taxes of Foreign Corporation.*—

(1) Treatment of Taxes Paid By Foreign Corporation.—For the purposes of this section, a domestic corporation which owns at least 10 per centum of the voting stock of a foreign corporation from which it receives dividends in any taxable year shall be deemed to have paid the same proportion of any income, war-profits, or excess-profits taxes paid or deemed to be paid by such foreign corporation to any foreign country * * * upon or with respect to the accumulated profits of such foreign corporation from which such dividends were paid, which the amount of such dividends bears to the amount of such accumulated profits. * * *

STATEMENT

The material facts are as follows:

In December, 1937, the petitioner caused its wholly-owned British subsidiary, Hoyt Metal Co. of Great Britain, Ltd. ("Hoyt Metal") to purchase from it a block of shares of Goodlass Wall and Lead Industries, Ltd. ("Goodlass Wall"), another British corporation. Those shares had cost the petitioner $1,677,970 and when sold were worth $1,288,939, at prevailing London Stock Exchange prices. The difference of $389,031 was treated by the petitioner as a deductible capital loss, which it offset against certain other gains which it had derived in the same year, 1937.

Hoyt Metal did not make immediate payment in cash for the Goodlass Wall stock it acquired. Instead, both petitioner and Hoyt Metal treated the amount due, some £257,884, as an indebtedness, on open account. Hoyt Metal also owed the petitioner certain other amounts, for a total of some £279,867. In 1938, 1939,

and 1940, Hoyt Metal reduced its debt to some £229,063. Except for a small adjustment, no further payments were made until 1952.

In the course of the 14 years after 1937, which embraced, of course, World War II and its difficult aftermath, Hoyt Metal had modest earnings. These were augmented by dividends received on Goodlass Wall shares, which Hoyt Metal retained for itself. On occasion, Hoyt Metal sold certain of the Goodlass Wall shares, and retained the proceeds for itself.

In 1952, the petitioner needed certain foreign exchange, specifically Deutschemarks, for its own corporate purposes. It met its needs by purchasing, on its own credit, British government bonds in the amount of some £228,613, the amount at which Hoyt Metal's indebtedness then stood. The petitioner promptly exchanged those bonds for Deutschemarks, and then caused Hoyt Metal to sell sufficient Goodlass Wall shares to enable Hoyt Metal to liquidate its indebtedness to the petitioner, which it did by remitting for the petitioner's account to the bank which had financed the petitioner's purchase of the British bonds.

When Hoyt Metal originally incurred its indebtedness in 1937, the pound sterling was worth nearly $5.00. When the debt was finally liquidated in 1952, the pound had been devalued, and stood at about $2.60. As a result, the petitioner received, in dollar value, considerably less than it would have received had the debt been paid with $5.00 pounds. The difference, some $568,755, the petitioner treated as a fully deductible foreign exchange loss in its tax return for 1952.

The Commissioner of Internal Revenue refused to allow the petitioner's claimed foreign exchange loss.

The Tax Court upheld the Commissioner, and its decision in this respect was affirmed by the Court of Appeals.

The Commissioner went further, however, and treated as dividends received directly by the petitioner, those paid by Goodlass Wall to Hoyt Metal. Additionally, the Commissioner treated as gains derived by the petitioner itself, those which Hoyt Metal received and retained from sales of Goodlass Wall shares. Here, too, the Tax Court upheld the Commissioner, and the Court of Appeals affirmed.

WHY THE WRIT SHOULD BE GRANTED

The writ should be granted because the Court of Appeals for the Second Circuit has decided an important question of Federal law which has not been, but should be, settled by this Court.

Importance of Question

The opening paragraph of Judge Marshall's opinion below, relevant to the issues as to which a writ of certiorari is sought by this petition, is as follows:

> The second and third issues in this case present interesting variations of a single theme: what consequences flow from the sale of property to a wholly-owned subsidiary, the loss on which sale is not deductible under the rule of *Higgins* v. *Smith*, 308 U.S. 473 (1940); *Crown Cork International Co.*, 4 T.C. 19 (1944), aff'd, 149 F. 2d 968 (C.A. 3, 1945); and *Bank of America N.T. & S.A.*, 15 T.C. 544 (1950), aff'd, 193 F. 2d 178 (C.A. 9, 1951). This question has, to our knowledge, not been presented to an appellate court heretofore.

As Judge Marshall says, the question here presented has not been before any other appellate court. Apart from its novelty, we submit that the question is of

sufficient importance to warrant this Court exercising its discretion to grant the writ (Rule 19).

The courts below have made a far-reaching and unwarranted extension of the principle of *Higgins* v. *Smith, supra.* Judge Atkins of the Tax Court said, in his opinion, expressing the ultimate basis for the Tax Court decision:

> * * *We think that the principle of *Higgins* v. *Smith, supra,* requires the conclusion that the transfer is to be disregarded or dismissed from consideration for *all* purposes of application of the taxing statute. (p. 303, Court's emphasis)

The Court of Appeals did not adopt Judge Atkins' language *in haec verba*, but its conclusions come to the same end.

In 1937, the petitioner sold certain shares of a British corporation to its wholly-owned British subsidiary, and claimed a "tax loss". That loss was allowed for 1937, though perhaps the principle of *Higgins* v. *Smith* (decided in 1940) would have been relevant. On the theory that *Higgins* v. *Smith* requires that the parties to a tax loss sale be regarded as never having entered into the transaction at all, the courts below held that:

> I. The petitioner is not entitled to a deduction for a loss, claimed for 1952, resulting from the fact that when the subsidiary finally liquidated the debt incurred in purchasing the shares in question, the British pound sterling had been devalued.
>
> II. The petitioner must include in its gross income for 1952 dividends received in that year by the subsidiary upon the shares in question, and gains from the sale by the subsidiary of some of the shares.

That this extension of the principle of *Higgins* v. *Smith* is far reaching is readily demonstrable. Until that case was decided, in 1940, tax loss sales to controlled entities were common enough. No doubt they began in 1909, in the case of corporations, and in 1913 in the case of other taxpayers. This means that if the Commissioner's agents can ferret out such a sale in *any* year since 1909, no matter how long the year has been otherwise closed, he can wreak havoc on long-established and bona fide relationships, by arbitrarily attributing ownership, and the tax consequences of ownership, to non-owners, in any open year, current or future.

The petitioner cannot, of course, prove statistically that, in due course, a large number of cases involving similar extensions of the principle of *Higgins* v. *Smith* will come before the courts. Yet, as is well-known, the ingenuity and energy of the Commissioner's agents and attorneys is productive—as it should be—of many issues and controversies, and it is hardly to be expected that they will not use the decisions below as tools of their trade. However, it would seem to be of substantial importance that they, and the lower courts concerned, should be instructed as to the true reach of *Higgins* v. *Smith*.

Policy of Repose

What has been said will at least suggest the basic juridical reason for review of this case: the principle or policy of repose. Ultimately, the time for controversy, for review, for revival of record and memory, must end, else the judiciary and the administrative machinery of the Government, and the citizens whom they serve, can ultimately be sorely pressed.

There is in this case no question but that when the controversy in this case arose, the statute of limitations with respect to 1952, the specific tax year involved, had not expired. Thus the petitioner cannot maintain that the Commissioner slept on his rights, as to 1952. Yet, it is in a sense shocking that the holdings below, in effect if not in full substance, rely upon a "reopening" of the tax year 1937, fifteen years prior to that directly involved, as to which the statute of limitations had long since expired.

We reiterate that as to 1952, the petitioner cannot urge a *statute* of limitations. We recognize, moreover, that *statutes* of limitation are creatures of the Congress. Yet, behind such statutes lies the *principle* of repose, which finds expression not only in Congressional enactments, but in decisions of this Court. We submit that the principle applies here.

In *Rothensies* v. *Electric Storage Battery Co.*, 329 U.S. 296 (1946), the taxpayer had paid certain excise taxes on electric storage batteries through and for the period April 1919 to April 1926. The statute of limitations for refunds for the April 1919 to April 1922 period expired before the taxpayer made a claim, but timely claims were filed for the April 1922 to April 1926 period.

In due course, in 1935, the 1922-1926 claims were allowed and refund was made. For the latter year, the Government claimed additional income taxes in respect of the refund. This claim was upheld, but the taxpayer countered with its own claim, for "recoupment" against the additional 1935 tax, the excise taxes overpaid for the 1919-1922 period. The lower courts held

for the taxpayer on this point. This Court reversed. The searching opinion by Mr. Justice Jackson included the following:

> This case represents an effort, thus far successful, to obtain advantage by way of recoupment of a claim for tax refund long since barred by the statute of limitations. The facts of *this singular situation* are not in dispute.
>
> * * *
>
> The gravity of this holding [by the lower courts] to the administration of the tax laws led us to grant certiorari. (pp. 298, 299, emphasis and brackets supplied)[1]

and further:

> It probably would be all but intolerable, at least Congress has regarded it as ill-advised, to have an income tax system under which there never would come a day of final settlement and which required both the taxpayer and the Government to stand ready forever and a day to produce vouchers, prove events, establish values and recall details of all that goes into an income tax contest. Hence, a statute of limitation is an almost indispensable element of fairness as well as of practical administration of an income tax policy.
>
> We have had recent occasion to point out the reason and the character of such limitation statutes. "Statutes of limitation, like the equitable doctrine of laches, in their conclusive effects are

---

[1] The Court pointed out that each of the two cases chiefly relied upon below, *Bull* v. *U.S.*, 295 U.S. 247 (1935), and *Stone* v. *White*, 301 U.S. 532 (1937), involved a single transaction or taxable event which had been subjected to two taxes on inconsistent legal theories, and what was mistakenly paid was recouped against what was correctly due.

designed to promote justice by preventing surprises through the revival of claims that have been allowed to slumber until evidence has been lost, memories have faded, and witnesses have disappeared. The theory is that even if one has a just claim it is unjust not to put the adversary on notice to defend within the period of limitation and that the right to be free of stale claims in time comes to prevail over the right to prosecute them." *Order of R. Telegraphers* v. *Railway Express Agency*, 321 U.S. 342. "They are by definition arbitrary, and their operation does not discriminate between the just and the unjust claim, or the voidable and unavoidable delay. They have come into the law not through the judicial process but through legislation." *Chase Securities Corp.* v. *Donaldson*, 325 U.S. 304.

As statutes of limitation are applied in the field of taxation, the taxpayer sometimes gets advantages and at other times the Government gets them. Both hardships to the taxpayers and losses to the revenues may be pointed out.* * * * (pp. 301, 302)

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* In *American Light & Traction Co.* v. *Harrison*, (C.C.A. 7th, Ill.) 142 F. 2d 639 * * *, the court did not allow recoupment to the Government. But, judiciously, it said, "Although here a hardship on the Government results from the taxpayer's inconsistency, the correlative provisions of this same statute will, in the converse of the instant situation, work an equal hardship on the taxpayer." 142 F. 2d 639, 643. Whether or not the statute, §§ 608 and 609 of the Revenue Act of 1928, be taken to compel the conclusion we reach in this case, the court's recognition that both parties to taxation are affected impartially, though perhaps harshly, by policy of repose has application here. * * *

The sound principle of ultimate repose which the *Electric Storage Battery, supra*, case expresses, we respectfully submit, was violated by the decisions be-

low. Those decisions do not accord with "the element of fairness" which is indispensable to practical administration of the tax laws. Perhaps, on its face, it does not seem unreasonable to some to ask a taxpayer to justify or explain what took place 15 years before the tax year in question, but much can be forgotten and lost in 15 years. The administrative necessity for review after 15 years and more have passed is, absent fraud, by no means obvious, and the simple justice of it even less so.

Duality of Jurisdiction

The property which was sold in this case consisted of shares of a British corporation; and the shares were sold to a British corporation. For many years the property sold, and the purchaser, were subject to British corporate law, to British property law, to British tax law, and to British foreign exchange law, and the like.

While the petitioner here would be unwilling to contend that a rule of law applicable to a British subsidiary of an American concern should be in any essential different from that applicable to an American subsidiary, we still wish to point out, as accentuating the incorrectness, impracticality, and injustice of the holdings below, the following:

(I) The loss claimed by the petitioner for the tax year 1952 was not attributable to the petitioner's action; it was not contrived; it was due solely and only to the devaluation of the pound sterling by the British

government, which, surely, was not "dominated and controlled" by the petitioner or its subsidiary.[2]

(II) Taxation directly to the petitioner of British dividends received and gains derived by its British subsidiary are not to be lightly dismissed by adverting to United States credits for foreign taxes. The subject of such credits for foreign taxes is intricate and complex, as a mere glance at section 131 of the Internal Revenue Code of 1939, which would apply to 1952, will demonstrate. There are many limitations. For example, no domestic corporation, such as the petitioner here, can have the benefit of the credit for taxes "deemed to have been paid", under section 131 (f) in respect of dividends paid by a British corporation unless the domestic corporation owns at least 10 per cent of the voting stock of the British corporation. Whenever the petitioner's "ownership" of Goodlass Wall voting shares drops below 10%, the petitioner is bound to be taxed by both the United Kingdom and the United States. The decisions below sanction such double taxation and thus, we submit, are plainly wrong.

CONCLUSION

The Court of Appeals for the Second Circuit has decided, erroneously, as the petitioner proposes to show, an important question of Federal law which has not been, but should be, settled by this Court.

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[2] Would the Commissioner concede that if devaluation had been by the United States, as in 1934, there would have been no "gain" in 1952, because "no debt existed"? Or is sauce for the goose not sauce for the gander, if the gander so chooses?

This petition for a writ of *certiorari* should be granted.

Respectfully submitted,

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